

September 16, 2005



# Financial Management

Review of the U.S. Army Corps of  
Engineers, Civil Works, Balance  
Sheet Reporting and Financial  
Statement Compilation  
(D-2005-108)

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Office of Inspector General

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### **Acronyms**

CEEMIS	Corps of Engineers Enterprise Management Information System
CEFMS	Corps of Engineers Financial Management System
CIP	Construction-In-Progress
COEMIS	Corps of Engineers Management Information System
DDRS-AFS	Defense Departmental Reporting System - Automated Financial Statements
GAO	Government Accountability Office
JV	Journal Voucher
MOA	Memorandum of Agreement
OIG	Office of the Inspector General
PP&E	Property, Plant, & Equipment
USACE	U.S. Army Corps of Engineers



INSPECTOR GENERAL  
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September 16, 2005

MEMORANDUM FOR COMMANDER AND CHIEF OF ENGINEERS, U.S. ARMY  
CORPS OF ENGINEERS

SUBJECT: Report on Review of the U.S. Army Corps of Engineers, Civil Works,  
Balance Sheet Reporting and Financial Statement Compilation  
(Report No. D-2005-108)

We are providing this report for information and use. We performed the review in response to a request from the U.S. Army Corps of Engineers. We considered management comments on a draft of this report in preparing the final report.

Comments on the draft of this report conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, no additional comments are required.

We appreciate the courtesies extended to the staff. Questions should be directed to Ms. Lorin T. Pfeil at (703) 325-5568 or Mr. Henry Y. Adu at (703) 325-6008. See Appendix H for the report distribution. The team members are listed inside the back cover.

By direction of the Deputy Inspector General for Auditing:

A handwritten signature in black ink, appearing to read "Paul J. Granetto", with a long horizontal line extending to the right.

Paul J. Granetto, CPA  
Assistant Inspector General  
Defense Financial Auditing Services

## Department of Defense Office of Inspector General

Report No. D-2005-108

September 16, 2005

(Project No. D2004-D000FE-0244.000)

### Review of the U.S. Army Corps of Engineers, Civil Works, Balance Sheet Reporting and Financial Statement Compilation

#### Executive Summary

**Who Should Read This Report and Why?** U.S. Army Corps of Engineers (USACE), Civil Works, management and personnel responsible for financial reporting should read this report. It discusses USACE, Civil Works, efforts to overcome impediments to reliable financial reporting.

**Background.** Since FY 2002, the DoD Office of Inspector General has conducted audits and assessments of the USACE, Civil Works, Balance Sheet reporting and financial statement compilation processes and has issued reports and memorandums identifying numerous deficiencies. On November 19, 2004, the USACE Chief of Staff asserted that corrective actions to remediate previously identified deficiencies had been implemented. The DoD Office of Inspector General was requested to review selected Balance Sheet line items and the financial statement compilation process to determine if the previously identified deficiencies had been corrected. The scope of the review was outlined in an engagement memorandum signed by USACE management and the DoD Office of Inspector General.

**Results.** USACE implemented numerous corrective actions to remediate previously identified deficiencies on the Civil Works selected Balance Sheet line items and with the financial statement compilation process. However, deficiencies continue to exist and Balance Sheet line items continue to be misstated. We found deficiencies in all six of the balance sheet line items we reviewed. Specifically, 309 of 853 sample items used to test for deficiencies failed our review. For the largest Balance Sheet line item reviewed, General Property, Plant and Equipment, we identified errors and unresolved audit issues totaling \$2.3 billion. In addition, we identified significant deficiencies with the financial statement compilation process including unsupported adjustments, undocumented differences in trial balance data, and inaccurate general ledger correlations. As a result of the continued deficiencies, we do not have reasonable assurance that the USACE, Civil Works, FY 2005 Balance Sheet is ready for an audit that would result in a favorable opinion. USACE needs to establish a comprehensive implementation program to ensure that the corrective actions to remediate previously identified deficiencies with the Civil Works Balance Sheet and financial statement compilation process are fully and consistently executed at all USACE activities. The program should include guidance for validation of corrective actions. In addition, the program should include a methodology for USACE headquarters to monitor the Balance Sheet reporting and financial statement compilation processes to ensure continued accuracy. (See the Finding section of the report for the detailed recommendations.)

**Management Comments.** The Commander of U.S. Army Corps of Engineers concurred with the finding and recommendation and stated that USACE has developed a “Get Well Plan” to achieve a clean audit opinion on USACE, Civil Works, FY 2006 Balance Sheet. See the Finding section for a discussion of management comments and the Management Comments section of the report for a complete text of the comments.

**Management Actions.** During the review, USACE headquarters held a workshop with representatives from DoD Office of the Inspector General and USACE field activities. The workshop provided guidance and discussed the responsibilities of the field activities personnel under the “Get Well Plan.”

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## Background

The DoD Office of Inspector General (OIG) performed this review of selected Balance Sheet line items and the financial statement compilation process at the request of USACE. We were not engaged to perform and did not perform an audit of the Balance Sheet items with the objective of expressing an opinion. Accordingly, we do not express such opinion. The determination of this review was based on the informational needs of the DoD officials who will use this report as part of the basis for deciding whether or not USACE, Civil Works, will be ready for an audit of its FY 2005 Consolidated Balance Sheet. See Appendix A for a discussion of the review scope and methodology.

**USACE Mission and Organization.** The USACE Civil Works mission is to manage water resource development as related to flood and coastal storm damage reduction, navigation, hydropower, recreation, water supply, regulation of obstructions in navigable waters and protection of the aquatic environment, environmental restoration and stewardship, and emergency response. USACE headquarters creates policy and plans future direction of all the other USACE activities. USACE is organized geographically into eight divisions and 41 subordinate districts that oversee project offices throughout the world. Additional USACE activities include a finance center, research and development laboratories, and other support activities.

**USACE Financial Reporting.** USACE, Civil Works, presents its total Assets, Liabilities, and Net Position on the Balance Sheet financial statement. USACE, Civil Works, uses three principal systems to prepare its financial statements. The Corps of Engineers Enterprise Financial Management System (CEFMS) is the official accounting and financial management system for USACE and is an interactive, on-line, and menu-driven database. During FY 1998, USACE completed the deployment of CEFMS to all of its divisions, districts, centers, laboratories, and field offices. CEFMS replaced the Corps of Engineers Management Information System (COEMIS). Consolidated financial data is reported from CEFMS to the Corps of Engineers Management Information System (CEEMIS). CEEMIS was developed by USACE to consolidate accounting data and to prepare reports. Financial data is compiled and transferred by general ledger account to the Defense Departmental Reporting System - Automated Financial Statements (DDRS-AFS). The DDRS-AFS is a DoD system that produces the USACE Financial Statements.

**Prior Deficiencies.** Since FY 2002, DoD OIG has conducted audits and assessments of USACE, Civil Works, Balance Sheet reporting and financial statement compilation processes and identified numerous deficiencies. The findings and recommendations related to these deficiencies have been published and communicated to USACE in numerous reports and memorandums. See Appendix B for prior audit coverage and Appendix C for a list of prior deficiencies.

**Memorandum of Agreement (MOA).** We identified the lack of documentation to substantiate the book cost for a significant portion of USACE, Civil Works, real property and the administrative costs associated with land as major audit

impediments in determining whether USACE, Civil Works, General Property, Plant, and Equipment (PP&E) is fairly stated. DoD OIG and USACE executed a MOA for developing alternate methods to estimate and support acquisition costs and capitalized improvements for real and personal property assets with remaining useful lives and administrative costs associated with land. In addition, the MOA described procedures to ensure that the Construction-In-Progress (CIP) costs that will be assigned to future assets are supported. The MOA represents the official baseline for supporting the book cost of individual USACE, Civil Works, General PP&E if properly executed. (See Appendix D for the Memorandum of Agreement.)

**USACE Information Papers.** USACE took action to correct deficiencies by issuing revised financial reporting policy in the form of 12 information papers (see Table 1). The information papers described the deficiencies identified by the Government Accountability Office (GAO), DoD OIG, and the U.S. Army Audit Agency and provided the necessary corrective actions to be implemented by USACE field activities. Most of the information papers required the responsible internal review office to validate completion of the corrective actions. However, the information papers did not provide any details on the scope and methodology to be used in conducting the validations. If properly implemented, the instructions outlined in the information papers should correct the significant deficiencies identified with the Balance Sheet line items and the financial statement compilation process.

<u>Information Paper</u>	<u>Subject</u>
1	Asset Cost Table Reconciliation
2	Construction-In-Progress
3	Abnormal General Ledger Balances
4	Project Relocation Costs
5	Accounts Receivable
6	Accumulated Depreciation
7	System Security Issues
8	Accounts Payable
9	Equipment
10	Buildings and Other Structures
11	Land
12	CEFMS General Ledger Correlations and Accounting Adjustments

The preliminary results of this review were briefed to USACE Headquarters personnel on March 8, 2005. In response, USACE held a workshop in May 2005 with representatives from DoD OIG and USACE headquarters and field activities. The workshop provided guidance on implementing the corrective actions set forth in the USACE information papers.

**USACE Management Assertions.** On November 19, 2004, USACE requested that DoD OIG review the implemented corrective actions to remediate previously

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identified deficiencies related to the selected balance sheet line items. USACE asserted that the corrective actions had been implemented and that USACE was ready for DoD OIG to perform a review. USACE asserted as of October 31, 2004, that the following actions had been completed.

- Information was presented in conformity with generally accepted accounting principles.
- Internal controls were established and maintained to provide reasonable assurances that internal control objectives are met.
- All material transactions in the accounting records underlying the Balance Sheet were properly recorded.
- All deficiencies related to the following Balance Sheet line items were corrected: Accounts Payable; Accounts Receivable; General PP&E (including Land; Buildings, and Other Structures; CIP; and Equipment), and Depreciation.
- Deficiencies related to the financial statements compilation process were corrected.

USACE asserted that the corrective actions adequately satisfied all Chief Financial Officer Act issues identified in previous USACE information papers and DoD OIG audit reports and memorandums. See Appendix E for the Management Assertion Memorandum.

**Engagement Memorandum.** On December 14, 2004, DoD OIG and USACE signed an engagement memorandum defining the purpose of the review. The engagement memorandum stated that previous audits of USACE, Civil Works, identified and documented deficiencies in the reporting of financial information for some USACE, Civil Works, Balance Sheet line items. The engagement memorandum communicated that the responsibilities of the DoD OIG included the performance of a review to express a conclusion about USACE assertions that corrective actions have been completed to eliminate the deficiencies. See Appendix F for the engagement memorandum.

## Objectives

Our overall objective was to determine whether USACE, Civil Works, had implemented corrective actions to remediate the previously identified deficiencies related to selected Balance Sheet line items. In addition, we reviewed the financial statement compilation process as required by the engagement memorandum. See Appendix A for a discussion of the scope and methodology and Appendix B for prior coverage related to the objective.

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## **USACE Implementation of Corrective Actions to Remediate Previously Identified Deficiencies**

USACE implemented numerous corrective actions to remediate previously identified deficiencies with selected USACE, Civil Works, Balance Sheet line items and with the financial statement compilation process. However, deficiencies continued to exist, and the balance sheet line items continued to be misstated. We found deficiencies in all six of the balance sheet line items we reviewed. Specifically, 309 of 853 sample items used to test for deficiencies failed our review. For the largest Balance Sheet line item reviewed, General PP&E, we identified errors and unresolved audit issues totaling \$2.3 billion. In addition, we identified significant deficiencies with the financial statement compilation process including unsupported adjustments, undocumented differences in trial balance data, and inaccurate general ledger correlations. The deficiencies continued to exist because USACE did not establish a comprehensive corrective action program to ensure that the instructions provided in its information papers were fully and consistently executed at all USACE activities. As a result of the continued deficiencies, we do not have reasonable assurance that the USACE, Civil Works, FY 2005 Balance Sheet is ready for an audit that would result in a favorable opinion.

### **Implementation of Corrective Actions**

USACE did not fully implement corrective actions to remediate previously identified deficiencies related to selected Balance Sheet line items. Specifically, 309 of 853 sample items used to test for deficiencies failed our review. For the largest Balance Sheet line item reviewed, General PP&E, we identified errors and unresolved audit issues totaling \$2.3 billion.

We reviewed the following USACE, Civil Works, Balance Sheet line items: Accounts Receivable, General PP&E (including Land; Buildings, Structures and Facilities; CIP; and Equipment) and Accounts Payable. The review was based on USACE's assertion that it had completed the necessary actions to correct all deficiencies identified in the Balance Sheet as of October 31, 2004. The audit teams considered the results of prior audits, date of last site visit, status of prior deficiencies, and availability and composition of universe data in determining the amount of coverage to provide for each line item. A combination of nonstatistical judgmental and simple random sampling techniques was used to select the sample items for review. The sampling methodology used for each line item is provided in Appendix A. The number of sample items reviewed for each Balance Sheet line item and the number of items found to have deficiencies are summarized in Table 2. The significant dollar value errors identified with General PP&E assets are summarized in Table 3. Details on the review are provided in separate paragraphs for each line item.

**Table 2. Overall Sample Item Results**

<u>Balance Sheet Line Item</u>	<u>No. Sample Items</u>	<u>No. Items With Deficiencies</u>
Accounts Receivable	120	10
Land	191	75
Buildings, Structures and Facilities	120	79 <sup>1</sup>
CIP	120	62
Equipment	160	46
Accounts Payable	<u>142</u>	<u>37</u>
<b>Totals</b>	<b>853</b>	<b>309</b>

<sup>1</sup> These items contained one or more deficiencies, which resulted in a total of 148 deficiencies.

**Table 3. Significant General PP&E Deficiencies  
(\$ in Millions)**

<u>Balance Sheet Line Item</u>	<u>Sample Errors</u>	<u>Other Errors<sup>1</sup></u>	<u>Unresolved Audit Issues</u>	<u>Total Deficiencies</u>
Land	\$482.8	\$ 2.9	\$ 0.0	\$ 485.7
Buildings, Structures and Facilities	105.9	0.0	0.0	105.9
CIP	86.2	815.6	835.3	1,737.1
Equipment	<u>0.5</u>	<u>0.0</u>	<u>0.0</u>	<u>0.5</u>
<b>Totals</b>	<b>\$675.4</b>	<b>\$818.5</b>	<b>\$835.3</b>	<b>\$2,329.2</b>

<sup>1</sup> Other errors include misclassified reservoir costs, non-Federal CIP, CIP errors identified during prior reviews, other completed CIP projects, CIP assets with negative balances, and variances between CIP general and subsidiary ledgers.

**Accounts Receivable.** USACE has taken action to ensure that receivables were recorded properly and the records maintained until the amounts due were collected or determined to be uncollectible, written off, or waived. USACE has also taken action to correct the recording of long-term agreements including reconciling to the general ledgers. However, USACE needs to improve the adequacy of source data and the reconciliation of the general ledger to the subsidiary records.

Of the 120 receivables sampled, USACE districts did not provide adequate source documentation for 10 receivables. Without adequate documentation, we were unable to determine if the receivables were recorded properly. This could impact the results of future audits that will not be limited to judgmental sampling. For example, a significant amount of current Accounts Receivable relate to District of Columbia Public Schools, which are reported by the USACE Baltimore district. The district continues to have difficulty providing adequate source documentation and a typical District of Columbia Public Schools receivable will have 10 to 50 separate lines of support. As of September 30, 2004, the current Accounts

Receivables line was valued at \$235.4 million and the District of Columbia Public Schools accounted for \$62.1 million (26 percent). The sample included one District of Columbia Public Schools receivable valued at \$5.4 million and the district could not provide support for \$0.4 million (7 percent).

The reconciliation of the September 30, 2004, trial balance to the subsidiary records identified numerous variances. USACE personnel at the district required a month to provide explanations, and this delayed the selection of the judgmental sample. USACE recognized the need to provide timely information and has since developed procedures to perform a reconciliation of the general ledger and subsidiary records prior to submitting the universe of Accounts Receivable for audit.

**Land.** USACE did not implement corrective actions for deficiencies involving land costs originating in COEMIS, land costs originating in CEFMS, and classification of reservoir costs. Of the 191 land records reviewed (97 COEMIS records and 94 CEFMS records) with a book value of \$2.0 billion, we determined that USACE had not completed corrective actions for 75 records valued at \$482.8 million. In addition, one USACE district did not properly record \$2.9 million of reservoir costs as Land. A break out of the deficiencies is provided in Table 4 and explained in the subsequent paragraphs.

**Table 4. Land Deficiencies**

<u>Type of Land Deficiency</u>	<u>No. Sample Items</u>	<u>Value (in millions)</u>
COEMIS Land Costs	52	\$480.3
CEFMS Land Costs	23	2.5
Misclassified Reservoir Costs*	<u>0</u>	<u>2.9</u>
<b>Totals</b>	<b>75</b>	<b>\$485.7</b>

\* These costs were not part of the review sample.

A sample of 97 COEMIS land costs, valued at \$2.0 billion, contained material and systemic deficiencies with supporting documentation, including data call spreadsheets. The corrective action required district personnel to separately identify the total land tract costs and total administrative costs for each property identification code and to identify the respective administrative cost components for each land asset. In addition, the corrective action required each district to prepare COEMIS to CEFMS conversion packages to provide alternative support documentation for COEMIS land cost. The conversion packages were to contain attestation statements signed by relevant district personnel, COEMIS to CEFMS conversion spreadsheets, and underlying corroborative documentation, to include COEMIS and Real Estate Management Information System printouts and USACE district Real Estate Division and Resource Management documents. Alternative supporting documentation for 52 items valued at \$480.3 million had one or more of the following exceptions: amounts were unsupported; variances existed between recorded values and underlying corroborative documents; administrative cost components were inaccurately identified; and, data call spreadsheets

contained miscellaneous variances. For example, one USACE district did not attest to COEMIS land costs for 18 of 19 items sampled. The costs were reported during a one-year period from the time the original attestation statements were signed until they were entered into CEFMS.

A sample of 94 land costs originating in CEFMS, valued at \$5.4 million, contained deficiencies with supporting documentation. The corrective action required district personnel to maintain complete supporting documentation for all CEFMS land costs in accordance with DoD policy. Land costs for 23 items valued at \$2.5 million were unsupported or had variances between the costs recorded in CEFMS and supporting documentation. For example, one USACE district improperly completed the data call spreadsheet, which precluded the testing of CEFMS land cost activity. The spreadsheet contained numerous duplicate disposal entries in the column indicating activity after the conversion from COEMIS to CEFMS. Also, CEFMS land cost activity was erroneously posted in the spreadsheet as being COEMIS land cost activity. Thus, we treated all 15 sample items involving CEFMS land cost activity as being in error.

One USACE district acknowledged that it did not reclassify reservoir costs totaling \$2.9 million from Buildings, Structures, and Facilities to Land as required by USACE Information Paper Number 10. The district indicated that it had overlooked the corrective action, but that it would make the necessary reclassifications of the affected accounts.

**Buildings, Structures, and Facilities.** USACE did not implement corrective actions for Buildings, Structures, and Facilities line item deficiencies involving useful lives, support for asset values, placed-in-service dates, asset classification (including bank stabilization), physical existence, and capital lease recording. Of the 120 CEFMS property records sampled with a book value of \$176.8 million, USACE had not completed corrective actions for 79 records valued at \$105.9 million. Each of the 79 records contained one or more of the deficiencies outlined in the following paragraphs. Considering that some items contained multiple deficiencies there were a total of 148 deficiencies as shown in Table 5.

<u>Type of Deficiency</u>	<u>Total Deficiencies</u>
Useful Life	48
Support for Asset Values	33
Placed-in-Service Date	26
Classification (Including Bank Stabilization)	20
Physical Existence	14
Capital Lease Recording	7
<b>Total</b>	<b>148</b>

Proper useful life values were not assigned in accordance with DoD and USACE policy. A total of 48 useful life deficiencies were identified. The corrective action required district personnel to review each assigned useful life value to

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ensure they do not exceed the maximum useful life allowable. Assets that were not unique to USACE, Civil Works, were reviewed to determine if the useful life complied with DoD policy. Assets that were unique to USACE, Civil Works, were reviewed to determine if the useful life complied with USACE policy. For example, one USACE district had not taken action to adjust useful life estimates. We found that all of their assets were assigned a 30-year useful life and were fully depreciated. However, the district had USACE-unique assets, such as dams, that should have been assigned a longer useful life and should not have been fully depreciated.

Documentation was not readily available to support the costs of assets. A total of 33 valuation support deficiencies were identified. The corrective action required district personnel to ensure that every asset had a supporting documentation file to include documentation for all integral costs from acquisition to disposal. We identified assets lacking third party supporting documentation for post-conversion assets and assets lacking documentation for some disposals.

Assets were not placed in service in a timely manner and placed-in-service dates did not match supporting documentation. A total of 26 placed-in-service date deficiencies were identified. The corrective action required district personnel to review and validate the accuracy of the placed-in-service date to an approved work order completion report and to ensure that the CEFMS placed-in-service date reconciled with the Real Estate Management Information System. For unrecorded assets identified during inventory or observation (referred to as “found on works” assets), district personnel must post the estimated placed-in-service date or the date the asset was found. At one USACE district, three assets found on works were not supported by the COEMIS to CEFMS conversion spreadsheet, third party documentation, or an engineering estimate.

Assets were not properly classified in 20 instances. The corrective action required district personnel to identify and reclassify assets that should be land, stewardship, heritage, equipment, or expense. We identified assets that should have been buildings instead of structures, an asset that should have been equipment, and assets that should have been expensed. One district reclassified heritage assets only if they were eligible for the National Register, rather than using the criteria outlined in the Federal Accounting Standards Advisory Board’s Statement of Federal Financial Accounting Standards Number 8. The same district erroneously classified moving boat docks as real property instead of personal property. The misclassified costs also included costs associated with bank stabilization that were not fully identified and removed. The corrective action required district personnel to determine whether the projects involve bank stabilization work. If a project involved bank stabilization, the asset had to be retired and disposed of in CEFMS. For example, one district had started to identify and remove bank stabilization costs from CEFMS but had not completed the corrective actions. We were unable to quantify the bank stabilization costs in service because the district pooled many individual asset costs into each property record and sufficient documentation was not on file to identify the bank stabilization costs.

Assets failed the physical existence testing because they were disposed, no longer in service, or impaired (not operating at full capability) and CEFMS records were not properly adjusted. A total of 14 existence deficiencies were identified. The

corrective action required district personnel to process approved disposal transactions, adjust assets to reflect current value based on current conditions, conduct inventories, and reconcile property records to the physical assets. At one USACE district, we could not trace individual assets to records in CEFMS.

Buildings and structures under non-Federal lease to local and State governments were not properly recorded. A total of seven capital lease recording deficiencies were identified. The corrective action required district personnel to review all leases and determine if the lease period exceeded 75 percent of the economic life of the buildings or structure. Furthermore, the USACE policy required districts to determine if the assets qualify as operating lease because the lease period begins in the last 25 percent of an asset's economic life. Assets under lease without a receivable were required to be transferred out and included in the lease as donations to the lessee. We identified assets at USACE districts that were under lease and should have been transferred out and assets under lease that were pooled with other assets within the same property records. Lease documentation at the districts had not been updated to include wording on transferring existing buildings and structures to the lessee for the period of the lease.

A systematic weakness was also identified involving adjustments to useful lives in CEFMS. Specifically, CEFMS does not always spread depreciation accurately across the life of structures, which affects the book value, accumulated depreciation, and ultimately, the balance of the Buildings, Structures, and Facilities line item. A CEFMS depreciation variance report identifies anomalies in the straight line depreciation calculation book value and the CEFMS recorded book value. Personnel at one USACE district used the depreciation variance report to identify the amount of adjustment needed after changing useful lives. Other visited districts had not made the necessary adjustments. This issue is being addressed with USACE as part of a separate audit project.

**CIP.** USACE did not implement corrective actions for CIP deficiencies, valued at \$1.7 billion, involving the timely transfer of completed assets, the capitalization of expense-type events, non-Federal cost share projects, prior CIP errors, negative CIP, and other variances. In addition, material audit issues relating to previously identified CIP deficiencies remained unresolved. Table 6 shows the deficiencies.

<u>Type of CIP Deficiency</u>	<u>No. Sample Items</u>	<u>Value (in millions)</u>
Federal CIP - Completed	44	\$ 68.1
Federal CIP - Expense-Type Events	18	18.1
Non-Federal CIP*	0	36.2
Prior CIP Errors*	0	462.0
Other Completed CIP Projects*	0	305.5
Negative CIP and Other Variances*	0	11.9
Unresolved Audit Issues	<u>0</u>	<u>835.3</u>
<b>Totals</b>	<b>62</b>	<b>\$1,737.1</b>

\* These were not part of the review sample.

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Of 120 Federal CIP assets sampled, valued at \$181.5 million, USACE had not completed corrective actions for 62 items, valued at \$86.2 million. The deficiencies involved the untimely transfer of completed projects and capitalization of expense-type events. A break out of the deficiencies follows.

- The uncorrected deficiencies included 44 items, valued at \$68.1 million, involving completed assets that had not been transferred out of CIP in a timely manner. The USACE CIP information paper requires that costs for completed assets should be transferred out of CIP and placed in service in a timely manner (30 days after completion). At one USACE district, 12 of the sample items reviewed were found to be in error because they consisted of assets that had been completed between FYs 1998 and 2004 and should have been transferred out of CIP.
- The deficiencies also included 18 items, valued at \$18.1 million, involving expense-type events that should not have been capitalized as CIP. At one USACE district, three items consisted of costs for studies that did not result in a capital asset and were erroneously recorded as CIP.

The CIP universe also contained \$815.6 million in other errors consisting of non-Federal cost share CIP (CIP identified by a non-Federal cost share control number in CEFMS), assets specifically identified as errors during prior reviews, completed CIP projects, and abnormal balances.

- Of \$164.4 million non-Federal cost share CIP reviewed, \$36.2 million was found to be in error. At one USACE district, the entire \$21.4 million CIP value related to four cost-share projects that involved work that would not be USACE-owned upon completion. The USACE CIP information paper requires that costs involving non-USACE-owned assets be expensed.
- CIP totaling \$462 million consisted of assets that were specifically identified as errors during prior CIP audits and remained uncorrected.
- At one sampled USACE district, CIP assets, valued at \$305.5 million, related to two major projects that had been completed and did not represent valid CIP. A DoD OIG audit team had previously identified one project as completed when they reviewed the Buildings, Structures, and Facilities line item. Another project was included as part of our review of non-Federal cost share CIP. Although the related assets were USACE-owned, work was completed in July 2004 and should have been transferred out of CIP.
- CIP assets with negative balances of \$9.0 million continued to exist and the CEFMS CIP subsidiary and general ledgers varied by \$2.9 million.

CIP unresolved audit issues related to USACE fish and wildlife mitigation programs and USACE Seattle district CIP were valued at \$835.3 million. DoD IG

Report No. D-2005-008, "Assessment of the USACE FY 2004 Beginning Financial Statement Balance of CIP," October 28, 2004, identified material deficiencies related to the Columbia River Fish Mitigation Program and the Wildlife Mitigation Land. In response to our final report, USACE stated that corrective actions would not be completed until June 30, 2005. In addition, during audit fieldwork for this review project, the USACE Seattle district indicated that it would not have the corrective actions completed until March 31, 2005. Therefore, we did not include the related CIP for the two USACE mitigation programs or the Seattle district CIP in our sample universe. However, we did summarize the related CIP balances as of October 31, 2004, to show their significance in relation to the overall CIP population.

**Equipment.** USACE did not implement corrective actions for deficiencies involving the lack of adequate documentation to support equipment values. We reviewed a sample of 160 equipment assets with a book value of \$15 million and determined that USACE had not completed corrective actions for 46 records valued at \$485 thousand. For example, one USACE district could not provide adequate documentation to support the values for 11 of the 20 equipment assets reviewed.

**Accounts Payable.** USACE districts did not correct previously identified internal control weaknesses involving Accounts Payable. The review revealed that USACE activities continued to improperly record payables, did not properly review aged payables, did not record payables in the proper accounting period, and were unable to provide supporting documentation in a timely manner. Of the 142 items sampled, 37 were improperly recorded. In addition, inadequate documentation was initially provided as support for 44 items, which resulted in additional data requests for sufficient documentation. A break out of the deficiencies is provided in Table 7.

<u>Type of Deficiency</u>	<u>Total Deficiencies</u>
Improperly Recorded Month-End Payables	24
Invalid Aged Payables	11
Payables Recorded in the Wrong Accounting Period	<u>2</u>
<b>Total</b>	<b>37</b>

USACE activities were not properly recording payables. Of 100 month-end payables sampled, 24 were found to be improperly recorded. These errors were due to payables being recorded before goods and services were received, payables being recorded twice, and lack of supporting documentation. For one sampled payable, funding was limited during continuing resolutions at the beginning of the fiscal year. As a result, an accrual up to the limit of funding was recorded, instead of the total amount of the accrual based on contractual obligations.

In addition, errors in the way CEFMS processed unfunded liabilities caused them to be overstated. We requested that USACE provide a list of all unfunded

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liabilities for contracts with the continuing contracts clause recorded as of the end of November 2004. USACE was unable to provide an accurate list because a CEFMS programming error was identified while working the data request. USACE personnel self-identified a CEFMS programming error which resulted in the footnote for unfunded payables to be grossly overstated on both the FY 2004 and first quarter FY 2005 financial statements. USACE personnel indicated that immediate corrective action was being taken and that scripts were written to correct the general ledger balances on all sites and the associated reconciliation programs were modified. USACE personnel stated that, because of the errors, a list of the transactions would not provide any usable information.

USACE activities were not properly reviewing aged payables. A separate sample of 26 aged payables (over 90 days old) was reviewed and 11 payables were found to be invalid. These errors were due to payables being entered twice, personnel not being adequately trained, miscommunication between USACE activities, and personnel not correcting data in CEFMS. One sampled aged payable was for flood control maintenance and the payable was deemed to be valid during the quarterly review in August 2004. However, our review revealed that the bill was paid to the contractor on July 25, 1997, and that it was not a valid payable. We concluded that USACE had not performed proper research during the quarterly review.

USACE activities continued to record payables in the wrong accounting period. A separate sample of 16 payables recorded in the first 15 days of the November 2004 accounting period was reviewed and two items were found in error. These errors were caused by personnel not recording the payables on the date the goods or services were received. One sampled payable was for engineering services provided through October 16, 2004. The contractor's invoice was dated on October 16, 2004, and was received on October 28, 2004. USACE personnel did not establish an accrual in October even though they had signed off that the job was completed. The cost of the completed services should have been accrued in October.

USACE activities also continued to provide inadequate supporting documentation. Of the initial sample of 100 month-end payables, 56 payables were at districts where the review was conducted by data call. For 44 of the 56 items, additional documentation had to be requested in order to adequately confirm the payables. The original support consisted of CEFMS reports, which did not provide adequate evidence of the receipt and acceptance of goods and services.

## **Financial Statement Compilation**

USACE improved the financial statement compilation process during FY 2004, but significant deficiencies continue to exist related to unsupported journal vouchers (JVs), and undocumented differences in trial balance data. In addition, USACE had not corrected the deficiencies with the CEFMS general ledger correlations.

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**Unsupported JVs.** Unsupported JV adjustments decreased from \$16.2 billion in FY 2002 to \$2.3 billion at the end of FY 2004. USACE created JVs to correct account balances, reverse prior adjustments, and ensure that data reconciled between financial statements. We reviewed 111 DDRS-AFS JVs valued at \$30.2 billion and determined that 20 JVs valued at \$2.3 billion were not supported. In addition, 18 JVs valued at \$7.6 billion were input erroneously, but were corrected with subsequent JVs. The DDRS-AFS JVs continued to be unsupported due to forced elimination entries, illogical adjustments, and inadequate documentation. For example, a JV valued at \$20.7 million was created to record an adjustment to current year purchases. The JV did not provide adequate documentation to explain the calculation and rationale for the adjustment. In addition, USACE personnel identified 15 non-DDRS-AFS crosswalk adjustments—each valued at more than \$10 million—that were reviewed. We found 4 of the 15 adjustments to be unsupported.

**Undocumented Differences.** Undocumented differences between trial balance data transferred from CEEMIS to DDRS-AFS decreased from \$3.1 billion (net) in FY 2003 to \$295.4 million (net) at the end of FY 2004. USACE personnel developed CEEMIS for the purpose of consolidating and preparing USACE-wide accounting data and reports. The DDRS-AFS is a DoD system used to prepare the financial statements for all DoD reporting entities. The trial balance produced by CEEMIS is manually entered into a crosswalk spreadsheet that is used to populate the DDRS-AFS import sheets. USACE personnel were unable to provide adequate supporting documentation for the undocumented differences between the CEEMIS trial balance and the data submitted to DDRS-AFS.

**CEFMS General Ledger Correlations.** CEFMS general ledger correlations were not updated to correct deficiencies in the Revolving Fund, Trust Funds, and Borrowing Authority. USACE general ledger correlations are accounting entries that automatically debit and credit corresponding CEFMS general ledger and U.S. Government Standard General Ledger accounts. Federal agencies are required to map U.S. Government Standard General Ledger information to the financial statements. The U.S. Government Standard General Ledger, released annually in the Department of Treasury Financial Manual, provides technical guidance to standardize Federal agency reporting. The USACE Finance Center has provided detailed descriptions of the necessary Revolving Fund correlations to Huntsville to facilitate the coding changes. The Revolving Fund correlation deficiencies are expected to be corrected by October 2005. The recoding of the Revolving Fund correlations has delayed the correction of the Trust Fund and Borrowing Authority deficiencies.

## **Validation of Corrective Actions**

USACE did not establish a comprehensive corrective action program to ensure that the instructions provided in its information papers were fully and consistently executed at all USACE activities. USACE issued a series of information papers containing corrective actions to remediate the previously identified deficiencies with selective Balance Sheet items, and most of the information papers required validation of the corrective actions by the responsible USACE Internal Review

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offices. However, USACE did not establish adequate procedures for validating completion of the corrective actions. In addition, USACE did not establish a process to monitor the effectiveness and consistency of the validations at its field activities. During our review, we found that the responsible Internal Review offices did not always perform validations or performed insufficient validations. Some Internal Review offices were either vacant or contained only one employee, making it difficult to accomplish the validations in a timely manner. The overall results of our review showed that 309 of 853 items reviewed still contained deficiencies, which is a strong indicator that improvements to the validation process are necessary. Unless USACE improves its validation process, we have no reasonable assurance that the validations will ensure that USACE activities have effectively implemented the corrective actions to remediate the previously identified deficiencies.

Of the 12 USACE information papers, 10 contained a statement that the responsible Internal Review office must validate the completion of the corrective actions. The other two information papers on Land and CEFMS general ledger correlations and accounting adjustments did not contain a statement requiring validation. USACE Headquarters did not provide any guidance on how to accomplish the validations so there were no standardized procedures for validating corrective actions to remediate the deficiencies. Validations were not performed at some of the districts. At the districts where the validations were performed, there was inconsistency in the scope and methodology for the validations.

We performed an analysis of the validation process for the largest Balance Sheet line item, Buildings, Structures, and Facilities. Personnel at the responsible Internal Review offices were interviewed at each of the six districts visited to determine the methodology used to perform the validation and to obtain the results of the validation. At three districts, validations were not performed because corrective actions were still being implemented at the time of our visit. At the other three districts, validations were performed and reports issued stating that the corrective actions were completed. However, we found problems with these reports. At one district, an insufficient validation was performed because the Internal Review office made an error reviewing leased property. At another district, the validation did not identify any discrepancies. However, that finding was not supported by the results of our subsequent review. At the remaining district, the validation consisted of a limited inventory check and did not determine whether all corrective actions required by the respective information paper had been implemented. Overall, our sample results for the Buildings, Structures, and Facilities line item showed that 79 of 120 items reviewed had deficiencies.

## **Conclusion**

USACE implemented numerous corrective actions to remediate previously identified deficiencies with selected USACE, Civil Works, Balance Sheet line items and with the financial statement compilation process. However, the results of our review show that 309 of 853 items reviewed (more than one out of every

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three) still had deficiencies. In addition, significant dollar errors were identified in the General PP&E line and with the financial statement compilation process. The 12 USACE information papers address the significant deficiencies with the Balance Sheet reporting and financial statement compilation processes and were a good initial step in the corrective action plan. However, USACE did not ensure that the corrective actions were fully and consistently executed at its field activities. Proper validation by the responsible Internal Review offices would help ensure that the corrective actions are properly implemented. In addition, USACE Headquarters should monitor the validation process to ensure that it is performed in a sufficient and consistent manner at all USACE activities.

## **Recommendation and Management Response**

**We recommend that the Commander, U.S. Army Corps of Engineers, establish a comprehensive corrective action program to ensure that the instructions provided in the information papers are fully and consistently executed at all U.S. Army Corps of Engineers activities. The program should include guidance for validation of corrective actions. In addition, the program should include a methodology for U.S. Army Corps of Engineers Headquarters to monitor the Civil Works Balance Sheet reporting and financial statement compilation processes to ensure continued accuracy.**

**Management Comment.** USACE concurred and stated that it has issued a “Get Well Plan” with detail steps to achieve a clean audit opinion on the USACE, Civil Works, FY 2006 Balance Sheet.

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## Appendix A. Scope and Methodology

The review was performed to determine whether USACE had implemented corrective actions to remediate previously identified deficiencies related to selected Balance Sheet items. The review was requested by USACE.

We performed the review at USACE headquarters and field activities from November 2004 through June 2005 in accordance with generally accepted government auditing standards. The review was accomplished using a combination of preliminary analytical testing, site visits, and data calls. We conducted tests at USACE activities and selected transactions for testing the corrective actions for which USACE asserted full implementation. The DoD OIG and USACE agreed that the use of judgmental sampling for the selection of USACE districts and transactions testing was an appropriate testing methodology for this review engagement. We used professional auditor judgment to assess the significance of the number and dollar value of exceptions identified for each line item in relation to the total number and dollar value of items sampled.

Our scope was limited to the review procedures set forth in an official engagement memorandum signed by the DoD OIG Assistant Inspector General for Defense Financial Auditing Service and the USACE Chief of Staff (see Appendix F). We did not review the Fund Balance with Treasury line item because a DoD OIG final report was issued in December 2004. The USACE management control program was not reviewed. The audit teams each included in their review a minimum of six judgmentally selected sites. For each balance sheet line, the combined dollar value of the sites selected for review represented at least 3 percent of the total line item population. In addition, the audit teams generally sampled a minimum of 120 items from each Balance Sheet line item. Some line items received more coverage than others based on the professional judgment of the team performing the review. The audit teams considered the results of prior audits, date of last site visit, status of prior deficiencies, and availability and composition of universe data in determining the amount of coverage to provide for each line item. A combination of nonstatistical judgmental and simple random sampling techniques was used to select the sample items for review. Details are provided in the following paragraphs describing the sampling methodology used for each line item. See Appendix G for a detailed list of USACE sites visited during this review.

**Accounts Receivable.** The September 30, 2004, Accounts Receivable universe was used for sampling purposes. The universe could not be drawn from October 31, 2004, because the data is only archived on a quarterly basis. Three separate universe files consisting of long-term, current, and work-in-progress comprised the Accounts Receivable balance at September 30, 2004. Six USACE districts were selected to visit and test for implementation of corrective actions. All six districts had transactions in each of the three categories of Accounts Receivable: long-term, current, and work-in-process. Collectively the six districts reported \$1.4 billion for accounts receivable, which represented

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## Appendix A. Scope and Methodology (Cont.)

67 percent of the \$2.1 billion Accounts Receivable universe provided for review. Each district had 20 receivables reviewed that consisted of eight long-term, eight current, and four work-in-process receivables. Four receivables from each of the six districts were judgmentally selected to be tested with at least one receivable from each of the three categories, and then 16 receivables were randomly selected, using a simple random sampling methodology provided by DoD OIG Quantitative Methods Division. In total, 120 sample items were reviewed with a value of \$837.3 million. Analytical procedures were performed to evaluate the aged, debt collection, and uncollectible accounts using the monthly aged receivables report. Analytical procedures were also performed to review the CEFMS long term agreements module by evaluating journal vouchers and reconciling to the Accounts Receivable trial balance on September 30, 2004.

**Land.** The September 30, 2003, Land universe was used for sampling purposes instead of the October 31, 2004, universe because of CEFMS access issues and because it was the cutoff date for the data call spreadsheets prepared by USACE districts to comply with Information Paper No. 11 and used by us to select our sample of CEFMS land cost values. The FY 2004 year-end balance for Land assets was not materially different from the FY 2003 year-end balance. Six USACE districts were selected to visit and test for implementation of corrective actions. Collectively, the six districts reported \$2.9 billion of Land, which represented 36 percent of the \$8.1 billion land universe provided for review. From the six districts, we selected and reviewed sample values for 97 COEMIS land cost items with a value of \$2.0 billion and sample values for 94 CEFMS land cost items with a value of \$5.4 million. In total, 191 sample items were reviewed with a value of \$2.0 billion. A combination of nonstatistical judgmental and simple random sampling techniques was used to select the sample items for review.

**Buildings, Structures, and Facilities.** The October 31, 2004, Buildings, Structures, and Facilities universe was used for sampling purposes. Six USACE districts were selected to visit and test for implementation of corrective actions. Collectively, the six districts reported \$4.3 billion (book value) of Buildings, Structures, and Facilities, which represented 28 percent of the total \$15.1 billion universe provided for review. A sample of 20 assets from each of the six districts was selected to be tested for implementation of corrective actions. The total book value for the 120 sample items was \$176.8 million. Four assets from each of the six districts were judgmentally selected to be tested, then the remainder of the assets at each of the six districts comprised the universe from which an additional 16 assets were randomly selected, using a simple random sampling methodology provided by DoD OIG Quantitative Methods Division.

**CIP.** The October 31, 2004, CIP universe was used for sampling purposes for all sites except the USACE Portland district. The December 31, 2004, CIP universe was used to select a sample at Portland because corrective actions were still taking place on October 31, 2004. Six USACE districts were selected to visit and test for implementation of corrective actions. Collectively, the six districts reported \$885.5 million of CIP, which represented 23 percent of the total \$3.9 billion CIP

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## Appendix A. Scope and Methodology (Cont.)

universe provided for review. Separate sample populations were created for cost share projects and direct Federal projects based on data element descriptions provided by USACE Headquarters. Cost shared projects were identified by a non-Federal "cost share control number" in CEFMS. In our prior review, we found that CIP assets identified by a non-Federal cost share control number were generally transferred to another agency upon completion and not placed in service as USACE-owned PP&E. Therefore, we performed a separate analysis on these assets for purposes of this review because of the high likelihood of error.

A sample of 20 Federal CIP assets (individual fund account numbers containing Federal CIP costs) from each of the six districts was selected to be tested for implementation of corrective actions. The total value for the 120 sample items was \$181.5 million. Overall, our methodology to select the 20 items at each site involved judgmental sampling to allow for us to cover the fund accounts with the largest CIP value and to cover as many unique projects as possible. Additionally, we excluded from our sample any fund accounts reviewed in our prior audits. We followed up on any fund accounts that were considered as errors in our prior reviews outside our audit sample of 120 items.

We also reviewed the material cost share CIP at four sites already selected for a site visit as part of the review of Federal CIP assets. The total cost share CIP value at these four sites was \$110.2 million. Additionally, seven districts were audited by data call because they reported material non-Federal cost share CIP values. The total cost share CIP value at these seven sites was \$56.1 million. In total, \$166.3 million of non-Federal cost share CIP was reviewed.

**Equipment.** The October 31, 2004, equipment universe was used for sampling purposes. Eight USACE districts were selected to visit and test for implementation of corrective actions. Collectively, the eight districts reported \$276.2 million (book value) of Equipment, which represented 43 percent of the total \$647 million equipment universe provided for review. A sample of 20 equipment assets from each of the eight districts was selected to be tested for implementation of corrective actions. The total book value for the 160 sample items was \$15 million. Four assets from each of the eight districts were judgmentally selected to be tested, then the remainder of the assets at each of the eight districts comprised the universe from which an additional 16 assets were randomly selected, using a simple random sampling methodology provided by OIG, DoD, Quantitative Methods Division.

**Accounts Payable.** The November 30, 2004, Accounts Payable universe was used for sampling purposes. The universe could not be drawn from October 31, 2004, as this data was unavailable due to the narrow window of time available to retrieve data from the monthly databases. USACE, Civil Works,, reported a \$506 million balance for Accounts Payable and intragovernmental accounts payable as of November 30, 2004. Based on prior audit results, wider coverage of the Accounts Payable line was required compared to the other line items. Specifically, prior reviews revealed that each district office was treating payables in a different way,

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## Appendix A. Scope and Methodology (Cont.)

with no central direction. Three separate judgmental samples were selected to test the Accounts Payable line. A total of 142 items were sampled.

The first sample was selected to determine whether the Accounts Payable balances at the end of November were properly recorded, in the correct amounts, and were valid payables. A random sample of 100 payables, with a combined value of \$1.9 million was selected from 42 sites. The 42 sites accounted for \$422.3 million (83 percent) of the total \$506 million Accounts Payable. Eight of those sites were judgmentally selected for visits and the remaining 34 sites were audited using a data call methodology.

The second sample was selected at the eight sites visited to test the validity of aged Accounts Payable that were more than 90 days old. A judgmental sample of 26 payables over 90 days old with a value of \$3.5 million was selected for review.

The third sample was selected for cutoff testing at the eight sites visited to determine whether transactions that occurred in the first 15 days of November were properly allocated to the November accounting month. A judgmental sample of two transactions at each of the eight sites was selected from the population of November transactions falling in the first 15 days of the month. A total of 16 payables valued at \$4.5 million were selected for review.

**Financial Statement Compilation.** The September 30, 2004, USACE, Civil Works,, Year-End Financial Statement data was used to review the compilation process. We reviewed three types of journal vouchers: DDRS-AFS adjustments, non-DDRS crosswalk adjustments, and DDRS trial balance change log adjustments. For DDRS-AFS adjustments, USACE has eight appropriation groupings, or adjusted trial balances, for general ledger trial balance reporting. We examined 109 DDRS-AFS JVs valued at or above \$10 million. We also reviewed the two highest dollar value adjustments in the appropriation grouping not represented in the 109 adjustments. The 111 DDRS-AFS JVs totaled \$30.2 billion and represented 99.4 percent of the total dollar value of the DDRS-AFS adjustments. For the non-DDRS crosswalk adjustments, USACE identified 15 adjustments of more than \$10 million that were reviewed. The DDRS trial balance change log contained 37 lines of adjustments valued at \$2.4 billion that were reviewed.

We also examined the compilation of the Year-End FY 2004 USACE Civil Works Financial Statements to determine whether any undocumented differences occurred during the transfer of the Civil Works data from CEEMIS into DDRS-AFS. Specifically, we traced values from the CEEMIS trial balance, plus any documented adjustments, to the final FY 2004 USACE, Civil Works,, Financial Statements contained in DDRS-AFS.

**Use of Computer-Processed Data.** Although we relied on the data from CEFMS, we did not evaluate the general and application controls during this review. We used CEFMS to obtain our universes for each of the selected balance

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## Appendix A. Scope and Methodology (Cont.)

sheet line items and financial statement compilation area that we reviewed for sampling purposes. We performed various tests to determine the accuracy and reliability of the data. We required originating source data to support the selected balance sheet line item values in CEFMS. GAO and U.S. Army Audit Agency audits concluded that the information in CEFMS could not be relied upon because USACE did not have adequate internal controls and, therefore, we did not rely on those controls during this review. However, not evaluating CEFMS general and application controls did not affect the results of our review.

**Use of Technical Assistance.** The OIG, DoD, Quantitative Methods Division provided assistance in selecting random samples of transactions to achieve representation without making any projections.

**GAO High-Risk Area.** GAO has identified several high-risk areas in DoD. This report provides coverage of the Financial Management high-risk area.

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## **Appendix B. Prior Coverage**

During the last five years, GAO, DoD OIG, and the U.S. Army Audit Agency have issued numerous reports discussing USACE, Civil Works,, balance sheet line items. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov>. Unrestricted DoD IG reports can be accessed at <http://www.dodig.osd.mil/audit/reports>. U.S. Army Audit Agency reports are restricted to military domains and to GAO.

### **GAO**

GAO Report No. GAO-02-589, "Information Security," June 10, 2002

### **DOD IG**

DoD IG Report No. D-2005-051, "Independent Examination of the Land Assets at the U.S. Army Corps of Engineers, Civil Works," April 6, 2005

DoD IG Report No. D-2005-046, "Independent Examination of the Rights to U.S. Army Corps of Engineers Buildings and Other Structures," March 25, 2005

DoD IG Report No. D-2005-035, "Existence of U.S. Army Corps of Engineers Buildings and Other Structures," February 15, 2005

DoD IG Report No. D-2005-026, "Reliability of U.S. Army Corps of Engineers, Civil Works, Fund Balance With Treasury and Unexpended Appropriations," December 28, 2004

DoD IG Report No. D-2005-016, "Independent Auditor's Report on the U.S. Army Corps of Engineers, Civil Works, Fiscal Year 04 Principal Financial Statements," November 8, 2004

DoD IG Report No. D-2005-008 "Assessment of the U.S. Army Corps of Engineers, Civil Works, FY 2004 Beginning Financial Statement Balance of Construction-in-Progress," October 28, 2004

DoD IG Report No. D-2004-107, "U.S. Army Corps of Engineers Financial Information imported into the Defense Department Reporting System – Audited Financial Statements," August 5, 2004

DoD IG Report No. D-2004-092, "Corps of Engineers Equipment Reporting on Financial Statements for FY 2003," June 22, 2004

DoD IG Report No. D-2004-063, "Controls Over U.S. Army Corps of Engineers Buildings and Other Structures," March 26, 2004

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## **Appendix B. Prior Coverage (Cont.)**

DoD IG Report No. D-2004-059, "Assets Depreciation Reported on the U.S. Army Corps of Engineers FY 2002 Financial Statements," March 16, 2004

DoD IG Report No. D-2004-044, "Subsidiary Ledgers at the U.S. Army Corps of Engineers," January 16, 2004

DoD IG Report No. D-2004-032, "Independent Auditor's Report on the U.S. Army Corps of Engineers, Civil Works, Fiscal Year 03 Principal Financial Statements," December 3, 2003

DoD IG Report No. D-2004-023, "Corps of Engineers Financial Management System Accounting Processes," November 18, 2003

DoD IG Report No. D-2004-017, "Reliability of Construction-in-Progress in the U.S. Army Corps of Engineers, Civil Works, Financial Statements," November 7, 2003

DoD IG Report No. D-2003-123, "Corps of Engineers Equipment Reporting on Financial Statements for FY 2002," August 20, 2003

DoD IG Report No. D-2001-067, "Inspector General, DoD, Oversight of the Army Audit Agency Audit of the FY 2000 U.S. Army Corps of Engineers, Civil Works Program, Financial Statements," February 28, 2001

DoD IG Report No. D-2000-093, "Inspector General, DoD, Oversight of the Army Audit Agency Audit of the FY 1999 U.S. Army Corps of Engineers, Civil Works Program, Financial Statements," February 28, 2000

DoD IG Report No. D-2000-087, "Inspector General, DoD, Oversight of the Army Audit Agency Audit of the Army's General Fund Principal Financial Statements for Fiscal Year 1999," February 14, 2000

### **Army Audit Agency**

Audit Report No. A-2002-0411-FFC, "Audit of The U.S. Army Corps of Engineers, Civil Works Accounts Receivable-Jacksonville District," September 4, 2002

Audit Report No. A-2002-0412-FFC, "Audit of The U.S. Army Corps of Engineers, Civil Works Accounts Receivable-Huntington District," September 4, 2002

Audit Report No. A-2002-0413-FFC, "Audit of The U.S. Army Corps of Engineers, Civil Works Accounts Receivable-Little Rock District," September 4, 2002

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## **Appendix B. Prior Coverage (Cont.)**

Audit Report No. A-2002-0414-FFC, "Audit of The U.S. Army Corps of Engineers, Civil Works Accounts Receivable-Omaha District," September 4, 2002

Audit Report No. A-2002-0415-FFC, "Audit of The U.S. Army Corps of Engineers, Civil Works Accounts Receivable-Philadelphia District," September 4, 2002

Audit Report No. A-2002-0416-FFC, "Audit of The U.S. Army Corps of Engineers, Civil Works Accounts Receivable-Sacramento District," September 4, 2002

Audit Report No. A-2002-0417-FFC, "Audit of The U.S. Army Corps of Engineers, Civil Works Accounts Receivable-Savannah District," September 4, 2002

Audit Report No. A-2002-0549-FFC, "Audit of The U.S. Army Corps of Engineers, Civil Works Accounts Receivable-Detroit District," September 4, 2002

Audit Report No. A-2002-0347-FFC, "U.S. Army Corps of Engineers FY 2001 Financial Statements, Civil Works (Accounts Payable--Credit Card Purchases)," August 23, 2002

Audit Report No. A-2002-0348-FFC, "U.S. Army Corps of Engineers FY 01 Financial Statements, Civil Works (Compilation And Adjustments)," August 23, 2002

Audit Report No. A-2002-0345, "U.S. Army Corps of Engineers FY 01 Financial Statements, Civil Works (Accounts Payable--Accruals)," August 23, 2002

Audit Report No. A-2002-0344-FFC, "U.S. Army Corps of Engineers FY 01 Financial Statements, Civil Works (Accounts Payable--Progress Payments)," August 23, 2002

Audit Report No. AA-02-142, "Fiscal Year 2001 Financial Statements, U.S. Army Corps of Engineers, Civil Works," February 8, 2002

Audit Report No. AA-01-359, "Audit of the U.S. Corps of Engineers FY 00 Financial Statements, Civil Works (Property, Plant, and Equipment Valuation)," June 28, 2001

Audit Report No. AA-01-346, "Audit of The U.S. Army Corps of Engineers FY 00 Financial Statements Civil Works (Construction In Progress)," June 28, 2001

Audit Report No. AA-01-187, "Fiscal Year 2000 Financial Statements U.S. Army Corps of Engineers, Civil Works," February 14, 2001

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## Appendix C. Prior Deficiencies

From November 2002 through April 2005, DoD IG issued numerous audit reports and memorandums that identified deficiencies related to the USACE, Civil Works, balance sheet and financial statement compilation process. In addition, we issued two audit reports that followed up on USACE general and application control deficiencies reported by GAO and the U.S. Army Audit Agency. This appendix consists of official deficiencies we deem as impediments to the financial statement compilation process and to the audit of the balance sheet.

### Accounts Receivable

DoD IG issued a memorandum that identified impediments to an audit of accounts receivable for information to aid in planning for auditable financial statements.

- USACE showed differences between CEFMS general ledger amounts and subsidiary ledger amounts because long-term agreements could not be entered in CEFMS.
- USACE districts were not performing reconciliations to ensure receivables agree with general ledger amounts and did not enter the current portion of the long-term receivables as short-term receivables.
- USACE did not use mandatory summary accounts for accounts and interest receivable.
- USACE did not take timely action to address write-offs for delinquent accounts.

### Land

DoD IG issued a memorandum and a report related to USACE land that contained recommendations for the following deficiencies.

- USACE Land line item included unsupported administrative costs and administrative costs at the property identification level that had no associated land purchase costs, donated land tracts that were not assigned a fair market value or were assigned an unsupported fair market value, and amounts recorded for land tracts were not supported or did not agree with supporting documentation.
- Costs associated with disposed land tracts and reservoirs may have been misstated.

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## **Appendix C. Prior Deficiencies (Cont.)**

### **Buildings, Structures, and Facilities**

DoD IG issued three reports related to USACE buildings, structures, and facilities.

- Controls over buildings and other structures were weak because established USACE guidance was not consistently implemented, properly instructed to employees, and strictly enforced.
- Weaknesses included inadequate real property inventory procedures, inconsistencies in capturing real property assets, and improper segregation of duties.
- Placed-in-service and retirement dates were often unsupported or improperly established in CEFMS.
- Proper useful lives were not always established in accordance with Engineer Regulation 37-2-10.
- Acquisition costs for structures were frequently not properly captured or supported by sufficient third party documents.

### **Construction-in-Progress**

DoD IG issued two reports related to USACE CIP.

- USACE could not support pre-CEFMS project costs.
- USACE capitalized expense-type items as CIP.
- USACE did not transfer costs for completed construction projects out of CIP in the proper accounting period.
- USACE could not properly reconcile CIP costs maintained in CEFMS to source data.
- USACE misreported costs relating to non-Federal cost share projects as CIP.
- USACE did not properly record fish mitigation studies and bank stabilization projects.
- USACE should correct negative CIP balances and imbalances between CIP general ledgers and cost records.

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## **Appendix C. Prior Deficiencies (Cont.)**

### **Equipment**

DoD OIG issued two reports related to USACE equipment that stated USACE could not provide all documentation needed to support the value of equipment assets because USACE did not properly implement their improved document retention policy.

### **Accounts Payable**

DoD OIG issued a memorandum that identifies internal control weaknesses that could have a material effect on the USACE financial statements.

- Accounts payable were not recorded as of the date that goods and services were received, regardless of whether budgetary resources were available.
- Instead, accounts payable were recorded as of the date recorded in CEFMS. Further, CEFMS is programmed to reject valid accounts payable for which related obligations have not been recorded.
- When goods and services were received, but related invoices had not been received, estimates for the amounts owed were not recorded as accounts payable for small dollar transactions.
- Small dollar amount payables were not estimated and recorded as accounts payable, although they existed.
- USACE did not record actual accounts payable for invoices received around the end of the fiscal year.
- Accounts payable resulting from work performed by contractors under Engineers Federal Acquisition Regulation Supplement clauses 52.232-5001 and 52.232-5002 were not recorded when incurred, but rather when the applicable contract lines were funded.

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## **Appendix C. Prior Deficiencies (Cont.)**

### **Financial Statement Compilation**

DoD OIG issued two reports related to the USACE financial statement compilation process.

- CEFMS does not process and summarize all accounting transactions in accordance with the USSGL.
- USACE does not have a process in place to ensure that the CEFMS general ledger correlations were promptly updated or that deficiencies were corrected.
- USACE does not have effective controls to ensure accounting information transferred from CEEMIS to DDRS AFS was reliable. Finance Center personnel made undocumented adjustments because DoD policy and Federal system requirements for making accounting adjustments were not adequately implemented.

# Appendix D. Memorandum of Agreement

JUN 9 2004

MEMORANDUM OF AGREEMENT  
SUPPORT FOR RECORDED BOOK COST OF GENERAL PROPERTY, PLANT,  
AND EQUIPMENT ASSETS  
U.S. ARMY CORPS OF ENGINEERS, CIVIL WORKS

**Purpose.** To develop alternate methods to estimate and support the acquisition costs and capitalized improvements for real and personal property assets with remaining useful lives and administrative costs associated with land. In addition, to develop procedures for ensuring that the construction-in-progress costs that will be assigned to the assets in the future are supported.

**Auditing Guidance.** The American Institute of Certified Public Accountants Statement of Auditing Standard (SAS) Number 31, "Evidential Matter," requires that sufficient, competent evidential matter be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under audit. The auditor's work consists of obtaining and evaluating evidential matter concerning the assertions in financial statements. Assertions are representations by management. Management assertions regarding the valuation of assets address whether the assets have been included in the financial statements at appropriate amounts.

**Accounting Guidance.** Statement of Federal Financial Accounting Standards (SFFAS) No. 6, "Accounting for Property, Plant and Equipment," defines general property, plant, and equipment (PP&E) as any PP&E used in providing goods or services. Major categories of PP&E generally include land, land rights, buildings, other structures, construction-in-progress, capital leases, and equipment. The accounting standard requires that all general PP&E be recorded at cost. Costs should include all costs incurred to bring the PP&E to a form and location suitable for its intended use. For general PP&E in existence before October 1, 1998 (the effective date of SFFAS No. 6), the standard allows for the use of cost estimates, if the historical cost information necessary to comply with the standard had not been maintained. In accordance with the standard, estimates shall be based on:

- cost of similar assets at the time of acquisition or
- current cost of similar assets discounted for inflation since the time of the acquisition.

DoD Regulation 7000.14-R, the "DoD Financial Management Regulation," volume 4, chapter 6, "Property, Plant and Equipment," August 2000, states that the dollar value assigned to an asset shall be supported by appropriate documentation. Documentation (original documents and/or hard and electronic copies of original documentation) should

## Appendix D. Memorandum of Agreement (Cont.)

be maintained in a readily available location, during the applicable retention period, to permit the validation of information pertaining to the asset, such as the acquisition cost, the acquisition date, and cost of improvements. Supporting documentation may include, but not be limited to, purchase invoices, sales and procurement contracts, Engineer Form 3013, "Work Order/Completion Report," construction contracts, work orders, and other such documentation generated independently of the entity in possession of the property. A combination of these documents is often required to validate information pertaining to the asset. Supporting documentation for land may include, but not be limited to, offers to sell, purchases, deeds, and condemnation files.

**Record Retention Requirements.** DoD Regulation 7000.14-R, "DoD Financial Management Regulation," volume 1, chapter 9, "Financial Records Retention," August 2000, states that all financial records, both paper and electronic, documenting the acquisition of DoD PP&E shall be maintained for at least the minimum period specified in the applicable General Records Schedule (GRS) issued by the National Archives and Records Administration (NARA).

**NARA Requirements for Real Property Records.** The NARA GRS No. 3, item 1 requires that records, other than abstract or certificates of title, relating to real property acquired after December 31, 1920, be retained until 10 years after unconditional sale or release of the government of conditions, restrictions, mortgages, or other liens. Records related to real property acquired prior to January 1, 1921, are not covered by the GRS and must be scheduled by submission of a SF 115 to NARA.

**NARA Requirements for Personal Property Records.** NARA GRS No. 3, item 3 requires that the routine procurement files (including contract, receipt, inspection, and payment) related to transactions (including construction contracts) other than real property that exceed \$2,000 be retained until 6 years and 3 months after final payment. Files pertaining to transactions, including construction contracts, at or below \$2,000 should be retained until 3 years after final payment.

**Army Guidance.** The Army record retention guidance is inconsistent. The Deputy Chief of Staff, Army G-4, recognizing the problem with conflicting guidance, revised Army Regulation 710-2, "Supply Policy Below the National Level," February 25, 2004, to require that source documentation for capital assets be kept by the property book office for the life of the asset. All other asset documentation is to be kept for 6 years. Engineer Regulation 37-1-29, "Financial Management of Capital Investments," November 30, 2002, requires that all capitalized asset files be maintained for 10 years after the disposal of the asset. However, Engineer Form 3013 and supporting documentation are to be maintained and disposed in accordance with Army Regulation 25-400-2, "The Army Records Information Management System (ARIMS)." The Director, U.S. Army Records Management and Declassification Agency develops ARIMS policy and procedures and administers the ARIMS program for the Deputy Chief of Staff, Army G-1. The U.S. Army Records Management and Declassification Agency's retention and disposal policy for property management refers to Army Regulation 710-2, Chapter 16 (draft),

## Appendix D. Memorandum of Agreement (Cont.)

Engineer Regulation 405-1-12, "Real Estate Handbook," states that all capitalized asset files will be retained for 6 years and 3 months after the disposal of the asset.

**Record Retention Agreement.** For real property placed in service after FY 1998, the U.S. Army Corps of Engineers (USACE) agrees to maintain all the documentation (original documents and/or hard and electronic copies of original documentation) in a readily available location for the life of the assets in accordance with NARA record retention requirements. For administrative costs associated with land acquired after FY 1998, USACE agrees that the districts must retain documentation supporting those costs in accordance with SFFAS No. 6, the DoD Financial Management Regulation, and NARA requirements. For personal property acquired after September 30, 2002, USACE agrees that the districts must follow SFFAS No. 6, the DoD Financial Management Regulation, and the NARA requirements for personal property records along with their own implementing policy.

### **PART I. REAL PROPERTY**

**Background.** The USACE uses several types of buildings and structures to perform its mission, such as dams, bridges, reservoirs, and locks. As of September 30, 2003, USACE reported that the acquisition value (book cost) of its general PP&E totaled \$44.3 billion. The major asset classes were buildings and other structures, \$31.1 billion; land, \$8.1 billion, construction-in-progress, \$3.8 billion; and equipment, \$1.2 billion. The DoD Financial Management Regulation requires that the owner maintain supporting documentation for assets in a readily available location during the applicable retention period. This permits the validation of information pertaining to the asset, including acquisition cost, acquisition date, and cost of improvements.

**The Problem.** The lack of documentation to substantiate the book cost of a significant portion of USACE real property assets and the administrative costs associated with land, is a major audit impediment to determining whether USACE, Civil Works, general PP&E is fairly stated. The primary reason for the unsupported costs was that USACE district offices did not maintain documentation long enough because of the conflicting guidance. In addition, for the real property amount reported on the financial statements, USACE did not have accurate subsidiary ledger information on the quantity, type, and value of buildings and other structures to support those costs.

To compensate for the lack of supporting documentation and subsidiary ledger information, USACE issued specific guidance on how the districts should estimate the acquisition cost of real property. USACE district work groups allocated the capitalized project costs, by feature of work, to each item in the real property inventory using available real estate, financial, and operations data. To the extent possible, costs associated with each feature of work were to be allocated to the individual items of real property that related to the feature. If appropriate data were not available or real estate costs did not agree with the accounting records, the work group was to use the cost data provided by the finance and accounting office and estimate the original acquisition or

## Appendix D. Memorandum of Agreement (Cont.)

construction cost of each item of real property. After assigning costs of all real property items in accordance with the accounting records, the Chairman of the Real Property Work Group or representatives of the district's Real Estate and Resource Management offices were responsible for signing an attestation statement. The attestation indicated that costs assigned to the individual items were based on actual real estate records, where available, and/or an estimated cost based on project cost/general ledger records in the Corps of Engineers Management Information System (COEMIS). Cost estimates assigned to the individual items were based on the professional judgment of the work group using the total costs reflected in each feature of work.

USACE developed procedures to ensure that the ledgers remained in balance and that the inventory data were entered into the Real Estate Management Information System (REMIS). At that time, USACE used REMIS as the subsidiary ledger. Beginning in December 1993, USACE began converting financial accounting records from COEMIS to the Corps of Engineers Financial Management System (CEFMS). USACE district offices completed the conversion of general ledger and detailed subsidiary information from COEMIS to CEFMS at different times. The last district office converted to CEFMS in March 1998. Unlike COEMIS, CEFMS accounted financially for individual real property assets by property identification code. At the time of conversion, USACE used the information from the REMIS and the COEMIS/CEFMS conversion spreadsheets to establish values for individual property identification codes and populate the general ledgers in CEFMS.

**Agreement.** All parties acknowledge that the dollar value assigned to an asset will be supported by appropriate documentation. SFFAS No. 6 and the DoD Financial Management Regulation allow the use of alternate methods to estimate and support the acquisition costs for real property assets with remaining useful lives for transactions occurring before October 1, 1998. This Memorandum of Agreement documents an agreement between the Office of the Inspector General of the Department of Defense (OIG DoD), the principal auditor for USACE, and USACE, in coordination with the General Accounting Office and the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer. The agreement is an alternate method to estimate and support the acquisition costs for real property with remaining useful lives, administrative costs associated with land, and procedures for ensuring that the construction-in-progress costs that will be assigned to assets in the future are supported.

USACE agrees that SAS Number 31, "Evidential Matter," requires that the auditor consider the nature, competence, and sufficiency of evidential matter presented by management. Evidential matter supporting the financial statements consists of underlying accounting data and corroborating information available to the auditor. For evidential matter to be competent, it must be both valid and relevant. For evidential matter to be sufficient and competent, the auditor must obtain information that forms a reasonable basis for an opinion.

USACE also agrees to disclose in the notes to its Civil Works financial statements that assets put in service prior to CEFMS did not have adequate external support thus

## Appendix D. Memorandum of Agreement (Cont.)

alternate agreed upon procedures were used. USACE will include the total number of asset (to include cost) put in service before deployment of CEFMS.

**Buildings and Other Structures.** The OIG DoD agrees that the use of COEMIS/CEFMS conversion spreadsheets could be used to support the book cost of the real property (buildings and other structures) in existence before USACE converted the asset to CEFMS. Consequently, the baseline date for each asset will vary depending upon when it was converted to CEFMS. Each spreadsheet must be accompanied by an attestation statement from USACE Real Estate and Resource Management personnel that indicates that costs assigned to the individual items were based on actual real estate records, where available, and/or an estimated cost based on project cost/general ledger records in the COEMIS. In lieu of original supporting documentation indicating the acquisition date, the conversion spreadsheet or other documentation supporting the spreadsheet could be used to support the placed-in-service date established in CEFMS. USACE based the conversion procedures on the premise that the accounting records in COEMIS reflected the actual cost of the projects and would eventually serve as the basis for assigning the cost of the project to the individual property identification codes. Consequently, when the USACE completes its work on obtaining conversion spreadsheets with attestation statements for each project, the OIG DoD plans to perform other analytical procedures that would be used to determine the reasonableness of the COEMIS cost information associated with converted projects and the costs assigned to high-dollar-value assets.

For those projects for which a conversion spreadsheet is available, but an attestation statement is not provided to the auditors, USACE will obtain and provide a written statement from Real Estate and Resource Management personnel in the responsible district offices. These district personnel will attest that the costs assigned to the individual items were based on actual real estate records, where available, and/or an estimated cost based on project cost/general ledger records in the COEMIS. USACE will also furnish an attestation statement as to the reasonableness of the placed-in-service date if the conversion spreadsheet or other documentation supporting the spreadsheet does not indicate an acquisition date. If the original COEMIS/CEFMS spreadsheets are not available, USACE will re-create the spreadsheets using the same information and methodology used to create the originals. USACE will then annotate on the spreadsheets "non-original" and attest to the information and the methodology used to re-create them. If it is impossible to re-create a new spreadsheet, then USACE agrees to obtain appraisals and/or engineering estimates for missing conversion spreadsheets. A written statement describing the estimating methodology should accompany the appraisals and/or estimates and be attested to by responsible Real Estate and Resource Management personnel. USACE will clearly identify the methods/basis used to compute the estimated cost for any asset for which the conversion spreadsheet is missing. If any costs cannot be supported with documentation, USACE agrees to either reduce the book cost of the building or other structure by the amount of the unsupported costs or track the unsupported amounts by property identification code. When USACE completes the work related to the unsupported book cost, the OIG DoD agrees to consider the risk associated with relying on the unsupported amounts in auditing the financial statements.

## Appendix D. Memorandum of Agreement (Cont.)

USACE agrees that acquisition costs initially recorded in CEFMS, capitalized improvements made to existing assets since the conversion spreadsheet was prepared, and increases in acquisition costs from those recorded on the COEMIS/CEFMS conversion spreadsheets will be supported by independent source documents as prescribed in Engineer Regulation 405-1-12, chapter 16. In instances where the required documentation cannot be obtained, USACE agrees to obtain appraisals and/or engineering estimates as detailed in the DoD FMR, volume 4, chapter 6, with a written attestation. If any costs remain that cannot be supported with documentation or by an appraisal or engineering estimate, USACE will either reduce the book cost of the building or other structure by the amount of the unsupported costs or track the unsupported amounts by property identification code.

Because the OIG DoD will review only the COEMIS/CEFMS conversion spreadsheets for 43 sampled projects, USACE agrees to determine the availability of COEMIS/CEFMS conversion spreadsheets and written attestation statements for the assets in the projects not sampled. USACE agrees to reconcile differences between what was recorded in COEMIS at the time of conversion and what was distributed to the individual property identification codes on the conversion spreadsheets for entry into CEFMS. For changes made to existing assets since the development of the conversion sheet and new assets placed in service since the conversion, USACE agrees to ensure that sufficient source documentation exists in files maintained by the respective districts to substantiate the book cost recorded in CEFMS. Source documentation, such as an appraisal, or a written attestation statement should support the acquisition cost of revolving fund real property assets. USACE agrees to maintain all the documentation (original documents and/or hard and electronic copies of original documentation) in a readily available location, for the life of the assets.

**Construction-in-Progress.** USACE agrees to establish and implement procedures by November 15, 2004, that require that COEMIS costs that are associated with assets still in construction-in-progress be supported before associated assets are placed in service. In the new procedures, the Engineer Form 3013 for each transferred asset will indicate the dollar value of the capitalized costs originating in COEMIS for which sufficient source documentation does not exist. The Engineer Form 3013 will also identify the costs that originated in CEFMS that are supported by original documentation. USACE will obtain and provide a written statement from responsible USACE district personnel attesting that the costs assigned to the individual property identification codes were based on actual costs, where available, and/or an estimated cost based on project cost/general ledger records in COEMIS. USACE will attach the written statement with the supporting documentation, such as the CEFMS cost detail ledger as of the date of the conversion, to the Engineer Form 3013. The written statement, supporting documentation, or the Engineer Form 3013 will describe the types of goods or services that are associated with the capitalized costs for which sufficient source documentation does not otherwise exist. If any costs cannot be supported using this methodology, the book cost of the building or other structure will be reduced by the amount of the unsupported costs.

## Appendix D. Memorandum of Agreement (Cont.)

**Administrative Costs Associated With Land.** Reportable land costs are composed of the cost to acquire land tracts and all costs necessary to bring a tract of land to a form suitable for its intended use. This includes the administrative costs. Administrative costs associated with land on the FY 2003 Civil Works Balance Sheet represent approximately 70 percent of the \$8.1 billion recorded value for land. As with other real property, supporting documentation is not available for most of these administrative costs. To identify the administrative cost component, USACE agrees to separately identify total land tract costs and total administrative costs for each property identification code per district by May 2004.

From each of the districts, USACE will request the FYs 1994 to 1998 conversion data, the associated COEMIS/CEFMS conversion spreadsheets, and the signed attestation statements for all projects. The attestation statements indicate that costs assigned to the individual items were based on actual real estate records, where available, and/or an estimated cost based on project cost/general ledger records in COEMIS. For missing FYs 1994 to 1998 conversion spreadsheets or attestation statements, USACE will re-create the spreadsheets using the same information and methodology used to create the original spreadsheets. USACE will then annotate on the spreadsheets "non-original" and attest to the information and the methodology used to re-create them. If USACE cannot reconstruct the conversion spreadsheets, USACE will write off the recorded amounts or provide valid estimates. For administrative costs associated with land acquired after its conversion to CEFMS, USACE agrees that the districts must retain documentation supporting those costs in accordance with SFFAS No. 6, the DoD Financial Management Regulation, and NARA requirements.

The OIG DoD agrees to accept the conversion spreadsheets with signed attestation statements as alternative documentation that will approximate actual costs for the pre-CEFMS unsupported administrative costs of land. The baseline date will vary for each item depending upon when it was converted to CEFMS. Because the COEMIS or conversion data is alternative documentation, USACE agrees to select a judgmental sample of the available conversion spreadsheets from a minimum of one project each at five Power Marketing Administration districts and five non-Power Marketing Administration districts. USACE engineers will then validate the accuracy of the conversion data used to estimate project cost on the selected projects. USACE will provide the engineer-validated estimates to the IG DoD auditors. USACE also agrees to disclose all unsupported administrative costs (those costs not supported by actual real estate records or estimates) in the financial statement notes.

USACE agrees to reconcile differences between what was recorded in COEMIS at the time of conversion and what was distributed to the individual items on the conversion spreadsheets for entry into CEFMS. For changes made to existing items since the development of the conversion sheet and new items placed in service since the conversion, USACE agrees to ensure that sufficient source documentation exists in files maintained by the respective districts to substantiate the administrative costs recorded in CEFMS. USACE agrees to maintain all the documentation (original documents and/or

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## Appendix D. Memorandum of Agreement (Cont.)

hard and electronic copies of original documentation) in a readily available location, for the life of the items.

### PART II. PERSONAL PROPERTY

**Background.** USACE uses several different types of equipment assets to perform its mission such as forklifts, trucks, cranes, barges, and boats. The equipment portion of PP&E generally includes assets with an acquisition value of \$25,000 or more. It does not include land, buildings and structures, and construction-in-progress. The net book value of equipment in the USACE principal statements in FY 2002 was \$650.8 million. The DoD Financial Management Regulation requires that supporting documentation for the assets be maintained by the owner in a readily available location during the applicable retention period. This permits the validation of information pertaining to the asset, including acquisition cost, acquisition date, and cost of improvements.

**Problem.** USACE did not maintain adequate documentation to support all of the values recorded in CEFMS for a significant number of items of equipment reviewed. This occurred because USACE had not developed the controls necessary to ensure personnel adhered to existing policies and procedures for retaining documentation and valuing assets in the absence of historical data. The valuation problem resulted in the audit conclusion that USACE could not adequately support about \$47.5 million of the \$650.8 million disclosed on the FY 2002 financial statements as the value of equipment.

**Agreement.** For personal property assets acquired as of September 30, 2002, USACE agrees, when original supporting documentation for personal property assets is no longer available, that the asset costs need to be determined and documented using acceptable methods of estimating costs. Acceptable procedures for valuing assets for which historical cost documentation is no longer available include:

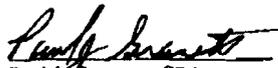
- appropriation or other Congressional information,
- Plant Replacement and Improvement Program documentation, if it can be used or adjusted to estimate the value of the assets at the time it was placed in service,
- estimated cost based on the cost of similar assets at the time of original acquisition, and
- current cost of similar assets, discounted for inflation since the time of acquisition.

USACE agrees to document the estimate on the USACE Internal Equipment Valuation (in Lieu of Supporting Documentation) form and have it certified by responsible personnel. For personal property acquired after September 30, 2002, USACE agrees that the districts must retain documentation supporting those costs in accordance with SFFAS No. 6, the DoD Financial Management Regulation, and NARA requirements.

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## Appendix D. Memorandum of Agreement (Cont.)

This Memorandum of Agreement, once agreed to by all parties, will represent the official baseline for supporting the book cost of individual USACE, Civil Works, general PP&E. The official baseline dates are not rolling baselines; therefore, alternative valuation methodologies for real and personal property will not be accepted for any transactions that occur after the asset's baseline period. The undersigned agree that this memorandum expresses our understanding of the actions that the OIG DoD and USACE agree to take.



Paul J. Granello, CPA  
Assistant Inspector General, Defense Financial Auditing Service  
Office of the Inspector General of the Department of Defense



Stephen Coakley  
Director, Resource Management  
U.S. Army Corps of Engineers

# Appendix E. Assertion Letter



DEPARTMENT OF THE ARMY  
U.S. ARMY CORPS OF ENGINEERS  
441 G STREET NW  
WASHINGTON, D.C. 20314-1000

19 NOV 2004

CERM-F (37)

MEMORANDUM FOR Office of the Deputy Inspector General for Auditing of the Department of Defense, Assistant Inspector General, Defense Financial Auditing Service Directorate, 400 Army Navy Drive, Arlington, VA 22202-4704

SUBJECT: Management Assertions Regarding Corrective Actions on the U.S. Army Corps of Engineers' Civil Works Balance Sheet

1. This memorandum asserts that the U.S. Army Corps of Engineers (USACE), Civil Works, has completed actions to correct all deficiencies identified in the Balance Sheet by the Office of the Inspector General of the Department of Defense (OIG DoD), as of October 31, 2004, except as indicated on the attached spreadsheet.
2. We hereby confirm, to the best of our knowledge and belief, that the following actions to correct the Balance Sheet as of October 31, 2004, have been completed, except for the weaknesses discussed in the enclosure.
  - a. We have fairly presented required information in conformity with generally accepted accounting principles.
  - b. We have established and are maintaining internal controls as of October 31, 2004 to provide reasonable assurances that USACE's internal control objectives are met.
  - c. We have properly recorded all material transactions in the accounting records underlying the Balance Sheet. There are no material events or transactions that have occurred subsequent to October 31, 2004, that have any material effect on our corrective actions.
  - d. We have corrected all deficiencies related to the following Balance Sheet line items: Accounts Payable; Accounts Receivable; General Property, Plant, and Equipment (PPE) (including Construction in Progress, Buildings and Structures, Land, and Equipment); and Depreciation. Also, we have corrected the compilation process of the financial statements. Our corrective actions addressed all Chief Financial Officer issues identified in the USACE information papers, deficiencies identified in the OIG DoD audit reports and memoranda, and the need for acceptable support for

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## Appendix E. Assertion Letter (Cont.)

CERM-F

SUBJECT: Management Assertions Regarding Corrective Actions on the U.S. Army  
Corps of Engineers' Civil Works Balance Sheet

recorded book cost of USACE Civil Works General PP&E agreed to in the June 9, 2004,  
Memorandum of Agreement signed by USACE and the OIG DoD.

FOR THE COMMANDER:

Encl.



JOHN R. McMAHON  
Colonel, Corps of Engineers  
Chief of Staff

# Appendix F. Engagement Memorandum



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-4704

DEC 14 2004

MEMORANDUM FOR COMMANDER, U.S. ARMY CORPS OF ENGINEERS

SUBJECT: Engagement Memorandum for the Review of the U.S. Army Corps of Engineers, Civil Works, Corrective Actions Related to Selected Balance Sheet Line Items (Project No. D2004FE-0244)

In previous audits of the U.S. Army Corps of Engineers, Civil Works (USACE) the Office of the Inspector General of the Department of Defense (OIG DoD) identified and documented deficiencies in the reporting of financial information on some USACE Balance Sheet line items (the deficiencies). The purpose of this memorandum is to establish an understanding of our engagement to review USACE corrective actions relative to the deficiencies.

## Auditor's Responsibilities

- We will perform a review to express a conclusion about USACE assertions that corrective actions have been completed to eliminate the deficiencies. A review engagement will provide a moderate level of assurance that our conclusions are correct regarding USACE assertions.
- The criteria we will use include generally accepted government auditing standards, incorporating the financial audit and attestation standards established by the American Institute of Certified Public Accountants (AICPA), as implemented by the GAO/PCIE Financial Audit Manual. The review will also include criteria such as DoD regulations and policies, Office of Management and Budget requirements, Statement of Federal Financial Accounting Standards, USACE policies and procedures and other applicable accounting requirements identified during the review. In addition, our review will include inquiries, analytical procedures, and limited transaction testing. We will meet with USACE management as needed to discuss our procedures, results of the review, and other issues of interest.
- During the review, we may consult with or depend on the work of actuaries, professional engineers, and internal auditors to obtain reasonable assurance of certain amounts on the financial statements. The OIG DoD will supervise all work conducted by specialists and internal auditors in support of our review, and all working papers prepared in support of the review will be OIG DoD property.
- If our report on the review engagement discloses deficiencies in internal control, fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse; we will obtain and report the views of responsible USACE officials concerning the findings, conclusions and recommendations, as well as planned corrective actions.
- OIG DoD work may result in one or more reports or memorandums intended for USACE information and use. As such, the information reported should not be used by those who have not agreed to the review or assumed responsibility for the

\*An assertion is any declaration or set of declarations made (in this case, by USACE) that the subject of the review is based on, or conforms to, the criteria selected for the engagement.

## Appendix F. Engagement Memorandum (Cont.)

sufficiency of USACE corrective actions. The reports and memorandums will be a matter of public record and we will not limit their distribution. Specifically, we will report on whether USACE performed corrective actions on the deficiencies. The OIG DoD will submit the draft report to the Commander of USACE about March 30, 2005.

### Management's Responsibilities

The U.S. Army Corps of Engineers, Civil Works, is responsible for:

- providing a written assertion letter stating whether the corrective actions to previously identified deficiencies related to selected Balance Sheet line items have been implemented and whether USACE is ready for the OIG DoD to begin their review work.
- assigning a primary and alternate point of contact (POC) that can be contacted to resolve questions or concerns between the OIG DoD auditors and USACE for each selected Balance Sheet line item. The POCs will be knowledgeable about the line item being audited and they should be able to make a decision for USACE. The selected Balance Sheet line items are Accounts Payable, Accounts Receivable, Property, Plant, and Equipment (to include Construction-in-Progress, Equipment, Land, and Buildings), Depreciation, and Fund Balance with Treasury. Also, Compilation of the Financial Statements will be reviewed.
- preparing and providing certain schedules and analyses of accounts, having available the requested documentation within 2 days of our request, and being available to answer questions posed by the OIG DoD audit teams.
- establishing and maintaining effective internal control over financial reports.
- identifying and ensuring compliance with applicable laws and regulations.
- making all financial records and related information available to OIG DoD auditors in a timely manner.
- providing a Management Representation Letter before the review report is issued.
- maintaining adequate audit trails and making system documentation, certification, and access to primary and feeder systems available to the auditors. Timely completion of this work will facilitate the completion of our review.

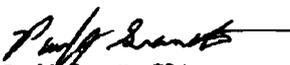
## Appendix F. Engagement Memorandum (Cont.)

### Additional Representation Concerning the Audit

The auditors and management agree that the auditor's use of judgmental sampling for the selection of USACE Districts and transactions for testing is an appropriate testing methodology for this review engagement. The nature of our transaction tests will vary depending on the particular Balance Sheet line item disclosure and the specific nature of the recommended corrective action(s).

Each OIG DoD line item audit team will conduct tests at selected USACE District Offices and select transactions for testing for each corrective action for which USACE management has asserted full implementation. The majority of our transaction testing will occur during the months of December 2004 and January 2005.

For additional information on this request, please contact Mr. Richard B. Jolliffe at (703) 428-1444 (rjolliffe@dodig.osd.mil), Mr. Steven K. Kurker at (703) 325-3549 (skurker@dodig.osd.mil), or Mr. Henry Y. Adu at (703) 325-6008 (hadu@dodig.osd.mil).

  
Paul Granetto, CPA  
Assistant Inspector General  
Defense Financial Auditing  
Service

Attachment  
as stated

If this memorandum, including the attachment, expresses your understanding, please sign below and return the original copy of the signed memorandum.

FOR THE COMMANDER:

  
Colonel John R. McMahon  
Chief of Staff  
U.S. Army Corps of Engineers

3 JAN 2005  
Date

## Appendix G. Sites Reviewed

USACE Activity	Accounts Payable	Accounts Receivable	Buildings and Other Structures	CIP	Equipment	Land	Financial Statement Compilation
Alaska District, AK	D <sup>1</sup>						
Albuquerque District, NM	D					V <sup>2</sup>	
Baltimore District, MD	D	D		D	V		
Buffalo District, NY	D						
Charleston District, SC	D						
Chicago District, IL				D			
Detroit District, MI	D						
Engineer Research and Development Center, MS	D						
Europe District, Germany	D						
Far East District, Korea	D						
Forth Worth District, TX	D	D	V			V	
Galveston District, TX	D						
Great Lakes and Ohio River Division, OH	D						
Humphreys Engineer Center Support Activity, VA	D						
Huntington District, WV	V				V		
Institute of Water Resources Division, VA	D						
Jacksonville District, FL	D	D		D <sup>3</sup>			
Japan District	D						
Kansas City District, MO	D	D				V	
Little Rock District, AR	V			V	V		
Los Angeles District, CA	V		V				
Louisville District, KY	D		V				
Memphis District, TN	D				V		
Millington District, TN							V
Mobile District, AL	D					V	
New England District, MA	D						
New Orleans District, LA	V			V			
New York District, NY	V			D <sup>3</sup>			
Norfolk District, VA	D						
Northwestern Division, OR	D						
Omaha District, NE	D						
Philadelphia District, PA	D	D			V		
Pittsburgh District, PA	D						

<sup>1</sup> Sites reviewed by data call are identified by a "D."

<sup>2</sup> Sites visited are identified by a "V"

<sup>3</sup> Sites visited but not included in sample.

## Appendix G. Sites Reviewed (Cont.)

USACE Activity	Accounts Payable	Accounts Receivable	Buildings and Other Structures	CIP	Equipment	Land	Financial Statement Compilation
Portland District, OR	V		V	V	V		
Rock Island District, IL	V			V			
Sacramento District, CA				D			
San Francisco District, CA	D			D			
Savannah District, GA			V				
Seattle District, WA	D			V	V		
South Pacific Division, CA	D						
St Paul District, MN				D			
St. Louis District, MO	D			V		V	
Tulsa District, OK	D	D	V	D		V	
Vicksburg District, MS	D			V	V		
Walla Walla District, WA	V			D			
Washington Aqueduct Division, DC	D						
Wilmington District, NC	D						
<b>Total Data Calls (D)</b>	<b>34</b>	<b>6</b>	<b>0</b>	<b>9</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total Site Visits (V)</b>	<b>8</b>	<b>0</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>6</b>	<b>1</b>
<b>Total Sites Reviewed</b>	<b>42</b>	<b>6</b>	<b>6</b>	<b>16</b>	<b>8</b>	<b>6</b>	<b>1</b>
<sup>1</sup> Sites reviewed by data call are identified by a "D." <sup>2</sup> Sites visited are identified by a "V."							

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## **Appendix H. Report Distribution**

### **Office of the Secretary of Defense**

Under Secretary of Defense (Comptroller)/Chief Financial Officer  
Deputy Chief Financial Officer  
Deputy Comptroller (Program/Budget)

### **Department of the Army**

Assistant Secretary of the Army (Financial Management and Comptroller)  
Assistant Secretary of the Army (Civil Works)  
Commander, U.S. Army Corps of Engineers  
Auditor General, Department of the Army

### **Department of the Navy**

Naval Inspector General  
Auditor General, Department of the Navy

### **Department of the Air Force**

Auditor General, Department of the Air Force

### **Non-Defense Federal Organization**

Office of Management and Budget

### **Congressional Committees and Subcommittees, Chairman and Ranking Minority Member**

Senate Committee on Appropriations  
Senate Subcommittee on Defense, Committee on Appropriations  
Senate Committee on Armed Services  
Senate Committee on Governmental Affairs  
House Committee on Appropriations  
House Subcommittee on Defense, Committee on Appropriations

# U.S. Army Corps of Engineers Comments



DEPARTMENT OF THE ARMY  
U.S. ARMY CORPS OF ENGINEERS  
441 G ST. NW  
WASHINGTON, D.C. 20314-1000

CEIR (36-2b)

13 August 2005

MEMORANDUM FOR Director, Defense Financial Auditing Service, Inspector General  
Department of Defense. 400 Army Navy Drive, Arlington, VA 22202

SUBJECT: Review of the U.S. Army Corps of Engineers, Civil Works, Balance Sheet  
Reporting and Financial Statement Compilation  
(Project No. D-2004-D000FE-0244.000) July 13-2005

The USACE response to the Department of Defense Inspector General (DoDIG) report  
recommendation follows:

**Recommendations.**

We recommend that the Commander, U.S. Army Corps of Engineers establish a comprehensive corrective action program to ensure that the instructions provided in the information papers are fully and consistently executed at all U.S. Army Corps of Engineers, Civil Works, activities. The program should include guidance for validation of corrective actions. In addition, the program should include a methodology for U.S. Army Corps of Engineers Headquarters to monitor Balance Sheet reporting and financial statement compilation processes to ensure continued accuracy.

**Command Response: CONCUR**

- (1) USACE developed a "Get Well Plan" in late March 2005. The "Get Well Plan" details the steps USACE will take to obtain a clean audit opinion on the USACE Civil Works FY06 Balance Sheet. The plan calls for all Regions to assert readiness no later than 30 Sep 2005.

FOR THE COMMANDER:

for:   
DONALD J. RIPP  
Chief, Audit Executive  
U.S. Army Corps of Engineers

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